STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 98-781

December 11, 1998

PUBLIC UTILITIES COMMISSION
Investigation of Standard Offer
Rate Design

STAFF PROPOSAL ON
STANDARD OFFER
RATE DESIGN

I. INTRODUCTION

The purpose of this document is to describe a proposal developed by Staff for determining the rate structures and customer class levels for standard offer electricity service. The proposal requires a flat cent-per-kWh rate design for residential and small commercial customers and allows the market to set rate design for all remaining customers through the standard offer bid process. In addition, the proposal allows the market to determine the rate levels of different customer groups independently. The proposal will require modification to the rate design terms of Chapter 301 of the Commission's Rules. Through this document the Commission solicits comment on the proposal.

II. BACKGROUND

Maine's electricity restructuring law (the Act) requires that standard offer service be available to all Maine consumers when retail access begins. 35-A M.R.S.A. § 3212. The Act directs the Commission to establish terms and conditions for standard offer service, and further directs that the service be acquired for Maine consumers through a Commission-administered competitive bid process. On February 11, 1998, the Commission provisionally adopted rules establishing the terms and conditions for standard offer service and the provisions governing the competitive bidding and selection process. *Order Provisionally Adopting Rule and Statement of Policy Basis*, Docket No. 97-739. Pursuant to the requirements for major substantive rules, the Commission submitted the provisionally adopted rule to the Legislature. The Legislature enacted a resolve modifying several provisions of the rule. On April 22, 1998, the Commission finally adopted Chapter 301.

Among the issues addressed by Chapter 301 is standard offer rate design. Specifically, in Section 2(A)(2) and (3), Chapter 301 provides that:

2. <u>Rate Structure</u>

Standard offer service rate classes, rate and usage elements, and daily and seasonal time-of-use periods shall be identical to the unbundled generation components contained in the rate schedules and terms and conditions of the core customer classes of each transmission and distribution utility as established by the Commission in the bill unbundling proceedings for each transmission and distribution utility pursuant to 35-A M.R.S.A. § 3213(1).

3. Rate Level; Rate Design

Rates for standard offer service shall be a uniform percentage, across and within customer classes, of each unbundled generation rate element of the core customer classes of the transmission and distribution utilities, as established by the Commission in the bill unbundling proceedings for each transmission and distribution utility pursuant to 35-A M.R.S.A. § 3213(1).

Chapter 301 § 2(A)(2) and (3). 35-A M.R.S.A. § 3213(1), referenced above, requires that the generation portion of utility bills be unbundled beginning in January 1, 1999. The Commission's rule implementing this unbundling provision provides that, for purposes of establishing standard offer rate structures, the Commission will establish unbundled generation rates and may use information from T&D utility rate proceedings for that purpose. Chapter 309 § 6(A).

On October 14, 1998, the Commission initiated this investigation to establish standard offer rate design as contemplated in Chapter 301. In the Notice of Investigation, the Commission noted that it had received few substantive comments on standard offer rate design during the development of Chapter 301 and stated its interest in reexamining the rate design provisions of the Chapter. In the Notice, the Commission requested comment on three potential rate design approaches. Two of the approaches deviate substantially from the design contemplated in Chapter 301 and would require the rule to be amended.[1]

In the Notice, the Commission stated that standard offer rate design might affect electric rate stability at the beginning of retail competition, transmission and distribution (T&D) utility rate design, and the ability of competitive electricity providers to operate competitively in Maine's retail generation market. In addition, in developing Chapter 301, the Commission stated two other goals: that standard offer service

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[1]These two approaches resulted from comments, made by CMP during its pending rate proceeding (Docket No. 97-580), that greater bidder flexibility in establishing standard offer class rate levels and rate design would be desirable.

should resemble traditional electric service and that standard offer bids should be easily and objectively comparable.

III. GENERAL CONSIDERATIONS

In developing this proposal, we weighed the important but often conflicting goals summarized in the Notice. These goals reflect the needs of customers, standard offer providers, other competitive electricity providers, and T&D utilities.

One goal is to maintain rate stability for standard offer customers at the beginning of retail competition; i.e., the combined rates of the T&D utility and standard offer providers should not, in and of themselves, cause serious bill impacts at the time of retail access. This goal implies that standard offer rate design and T&D rate design will be dependent on one another. For example, after a standard offer rate design is determined, the T&D rate elements will be calculated as residuals from current utility rates.

A second goal is to establish a standard offer rate design that allows the Commission to promote cost-based T&D rates. For example, some commenters suggested a flat kWh rate that is not time-of-day or seasonally differentiated as the standard offer rate design. That design, however, would cause a greater disparity between T&D rates and T&D costs if, on a combined basis, overall electric rates remained unchanged. Conversely, flat rates, when combined with cost-based T&D rates, would reduce overall rate design stability at the beginning of retail competition.

A third goal is to match standard offer rates closely to standard offer costs, to minimize the revenue risk faced by standard offer providers and thereby encourage a larger bidding pool and lower bid prices. This matching is difficult to guarantee through an administrative solution when the generation market is immature. Allowing marketers to establish their own potential cost structures and levels for each group of customers might allow bidders to feel more confident that their revenues will reflect their costs. However, the approach introduces the risks that disproportionately low standard offer rates would inhibit some customer groups from migrating toward the competitive market or that disproportionately high rates would exist for other customers. The approach might also make it difficult to establish objective selection criteria.

IV. PROCEDURE FOR DETERMINING RATE STRUCTURES AND LEVELS

After consideration of these goals, the Staff proposes the following terms and procedures for standard offer rate design:

1. For each T&D service territory, there will be three *standard offer rate classes*:

a. residential/small commercial;
b. medium commercial/industrial (C/I); and
c. large C/I.

The breakpoint between small and medium C/I will not exceed 50kW and will be the breakpoint used to define load profile groups pursuant to Chapter 321. The breakpoint between medium and large C/I will not exceed 500kW and will be the breakpoint used to define load profile groups pursuant to Chapter 321.

2. Bidders may bid on one, two, or all standard offer rate classes.

3. For the residential/small commercial class, bidders must bid (and customers will pay) a single price per kWh for all times of year, for the term of the bid.

4. For the medium and large C/I classes, bidders may bid (and customers will pay) based on rate components or time-of-use prices that are compatible with the T&D utility's rate designs[2] for those customers.[3]

5. For the residential/small commercial classes, bidders must follow the procedures for bidding on portions of total class service contained in Section 7(B)(4) of Chapter 301.

6. For the medium and large C/I classes, bidders must follow the procedures for bidding on portions of total class service contained in Section 7(B)(4) of Chapter 301, but must also include a bid for 100% of total class service.

7. Winning bidders will be chosen for each standard offer rate class independently of the choice made in the other two classes.

8. The Commission will select more than one winning bidder for a class if:

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[2]A standard offer rate class might encompass more than one T&D rate class. The standard offer rate design must be compatible with all the T&D rate designs it encompasses.

[3]For example, if the T&D rate structure includes both an energy and a demand charge, bidders may bid standard offer prices comprised of energy and demand charges, or they may bid energy charges only. If the T&D rate structure is time-of-day differentiated, the bid may differentiate by identical time periods, or it may be non-time-differentiated.

a. the choice will not raise total rates to that class by more than 0.5%; and

b. the rate structures of the bidders may be blended into a single rate structure in a manner that creates reasonable relationships among rate elements.

9. Winning bidders will be paid the price they bid. Standard offer customers will pay rate elements calculated by weighting the bid of each winning provider by the percentage of the total class usage awarded to that provider.

10. For the medium and large C/I classes, the rates of multiple providers will be blended to create a single standard offer rate structure in a manner that preserves reasonable relationships between rate elements. The resulting rate structure will be determined by the Commission after reviewing the rate structures of the winning bidders.

11. To compare bids for the medium and large C/I classes, the average rate for each bid will be determined by applying the bid rates to class billing units in the year preceding the bid.

Furthermore, we recommend that the duration of the initial period of standard offer service be one year rather than two years as currently provided in Chapter 301.

V. DISCUSSION

Many commenters recommended that standard offer rate classes be highly aggregated. We agree. Most T&D rate class differentiation is more refined than necessary to reflect supply costs. In fact, for most customers, supply costs will be largely determined by the profile groups defined in Chapter 321 for load settlement purposes.[4] Therefore, the proposal establishes three standard offer rate classes that are consistent with the load profile groups.

For larger customers, the proposal departs from the administrative determination of unbundled generation rate structure contemplated by Chapter 301. Arguments that it will be difficult to predict generation price structures or relative customer class levels in the early stages of market development are persuasive. By allowing bidders to predict their own cost structures, the risk of estimation is transferred to the

[4] This is because settlement with the bulk power system administrator will place all non-telemetered customers in one of three customer groups, and will assign the same hourly load curve to all customers in a group.

providers whose business success will be affected by the prediction. This approach should result in lower bid prices than would the administrative approach. The proposal maintains an administrative requirement that the residential/small commercial structure be a single cent-per-kWh. This structure will be easy for customers to understand and will allow for objective bid evaluation.

Commenters identified benefits and risks to allowing bids on less than the total standard offer customer base (i.e., on a single rate class). There is concern that eliminating the guarantee of serving such a potentially large and diverse market will make standard offer service less attractive to bidders. There is also concern that there may be no bids, or artificially high bids, for one or more standard offer rate class. On the other hand, allowing separate bid prices for each of the three proposed rate classes should improve a bidder's ability to match costs to revenues. If separate class bids are allowed but a provider is also required to bid on the full customer base, it will be difficult to evaluate competing bids. Therefore, the proposal is to evaluate bids on each class separately. If no bid is received for one or more rate classes, we anticipate the Commission will reevaluate the situation consistent with 35-A M.R.S.A. § 3212(3).

The proposal retains Chapter 301's provision allowing the Commission to choose more than one winning bidder. However, we recognize that allowing bidders to determine their own rate design might make it difficult to blend two providers' bids into a single rate structure that customers would pay. The proposal contemplates that multiple providers within a class will not be chosen if their widely disparate rate designs create a blended structure that is unreasonable by some cost-based or market-based criterion.[5] Because of this problem, it is possible that only one provider will be chosen to serve the medium C/I or the large C/I classes. However, if two low-price bidders offer rate designs that can reasonably be blended, the proposal would allow this to occur.

The proposal retains the intent of Chapter 301's provision that providers bid on multiples of 20% of total usage by applying

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[5]For residential and small commercial customers, the single standard offer rate will be calculated by weighting the cent-per-kWh bid of each winning provider by the percentage of the total class usage awarded to that provider. However, it is problematic to calculate a single (or "blended") standard offer rate from multiple bids that feature disparate rate designs. For example, if one provider offers time-of-use rates with no demand charge and a second provider offers flat rates with a demand charge, the benefits of both forms of price differentiation might be unacceptably diluted by blending the rates.

the provision to each rate class separately. However, because it might be impossible to choose multiple providers for the medium and large C/I standard offer rate classes, the proposal adds the requirement that bidders for these two rate classes be willing to serve the entire class and, accordingly, to include a bid of 100%.

VI. PROCESS FOR COMMENTS

A technical conference on this proposal will be held on January 8, 1999, at 1:00 at the Public Utilities Commission. Written comments on the proposal may be filed with the Administrative Director no later than January 5, 1999. The Commission requests that parties submit comments regardless of whether the commenter has intervened or submitted earlier comments in this proceeding. Written comments should refer to the docket number of this proceeding, Docket No. 98-781, and be sent to the Administrative Director, Public Utilities Commission, 242 State Street, 18 State House Station, Augusta, Maine 04333-0018.

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